



Telephone:
(916) 445-0255

STATE OF CALIFORNIA
Office of the Auditor General
660 J STREET, SUITE 300
SACRAMENTO, CA 95814

Kurt R. Sjoberg
Acting Auditor General

October 15, 1990

P-032

Honorable Elihu Harris, Chairman
Members, Joint Legislative
Audit Committee
State Capitol, Room 2148
Sacramento, California 95814

Dear Mr. Chairman and Members:

We have completed a preliminary review of the Martin Luther King, Jr. Community Plaza project in order to determine the extent of work needed for a full scope audit. Based upon this preliminary review, we recommend that the Joint Legislative Audit Committee amend the original audit request to focus our work on the feasibility of refurbishing the historical buildings and the economic viability of the city's various options.

BACKGROUND

The University High School, located on what is now Martin Luther King, Jr. Way in North Oakland, was built in 1923. The main building is a two-story stucco-clad structure, with an Italian Renaissance influence. In 1946, the school was converted to the Merritt School of Business and the Joseph P. Laney Trade and Technical Institute, which is commonly known as the Old Merritt College. In the early 1980s, after the Oakland Unified School District determined that it no longer had a need for the facility, the City of Oakland (city) purchased the facility for approximately \$460,000. The city used Community Development Block Grant funds that it received from the federal government via the Department of Housing and Urban Development (HUD) to purchase the site. The main building, including the auditorium, and the gymnasium meet the eligibility criteria for the National Register of Historic Places.

In 1982, the city issued a request for proposals to develop the nine-acre site into a community center for office, cultural, retail, health, education, and recreational activities. The request for proposals specified that proposed projects retain both the main building and the gymnasium. According to a chronology prepared by city staff, the city rejected the two development proposals it received in April 1982.

Since that time, the city has entered into a series of agreements with a number of consultants and developers to try to develop what is now known as the Martin Luther King, Jr. Community Plaza project. For example, in 1984, the city received a development proposal from one developer. The city entered into a series of agreements with this firm to provide a development plan, including an analysis of the buildings, market and feasibility studies, and a financial analysis, among other services. The firm submitted its final report in May 1986. This report recognized the possible historical significance of the main building and the gymnasium and included an application to the National Park Service for historic preservation certification for the two buildings. However, the city ultimately terminated its negotiations with the firm.

In September 1986, the city contracted with a consultant to assist in designing a community participation process and to develop a new request for proposal. This consultant recommended that the city retain and renovate the auditorium and a portion of the west wing of the existing main building, but remove the rest of the main building and all other buildings on the site, including the gymnasium. According to the city's chronology, it held a series of community meetings from September 1986 through October 1987 to obtain the community's input for the development process.

In September 1987, the city issued a request for developer qualifications (RFQ). Again, the city received only two responses, but it selected one of the developers. This selected developer presented a revised site plan that called for demolition of all of the buildings on the site. The city's RFQ process, the developer, the developer's plan, and the physical condition of the facility have become the center of a community controversy. As of October 4, 1990, the main building and the gymnasium are still standing on the site although the city demolished several portable structures. In addition, the city has not adopted a final project plan, although the developer plans to present a new plan to the public on October 19, 1990.

In June 1990, the Joint Legislative Audit Committee requested the Office of the Auditor General to review the circumstances surrounding the development project and assess the project's viability. On August 13, 1990, the city's manager wrote to the Joint Legislative Audit Committee, objecting to a state audit because the city did not use state funds for the project. The city manager listed the actions the city has taken and cited reviews already performed by the city's auditor and the HUD (see Attachment).

In our preliminary review, we met with representatives of the city's Office of Economic Development and Employment, the State Office of Historic Preservation, and the HUD's Office of Inspector General. We reviewed files related to the project at all three of those offices. In addition, on October 2, 1990, we visited the site in the company of city staff and an auditor from HUD's Office of Inspector General. Although there has not been enough time to answer all the questions raised by the audit request or to confirm all of the city manager's assertions, we have completed a preliminary review and provide the following information to the Joint Legislative Audit Committee.

RESULTS OF THE PRELIMINARY REVIEW

We gathered preliminary information on the five issues raised by the City of Oakland in its August 13, 1990, letter to the Joint Legislative Audit Committee. The five issues are:

- Whether it is economically feasible to refurbish the main building and auditorium;
- Whether the property is adequately protected from vandals and deterioration;
- The ability of the developer to complete the contract;
- Whether it is in the best interest of the city to grant more time to the developer to complete the project, to issue a new RFQ, or sell the property; and,
- Whether the city's RFQ process was adequate.

The results of our data gathering follows.

Whether It Is Economically
Feasible To Refurbish the
Main Building and Auditorium

Based on our preliminary review, which did not include a thorough cost analysis, it appears to be economically feasible to refurbish the main building and auditorium. The city manager stated that consulting engineers concluded that it was not feasible to refurbish the main building for retail use. While the city has included retail space in its definition of the project since as early as 1982, the early definition of the project also included office, cultural, health, educational, and recreational uses. Nevertheless, the city's priorities have changed over time. As early as January 1988, the city had discussions with Children's Hospital about developing a project that would include the hospital's needs. These discussions continued through March 1990. At least one of the plans allowed Children's Hospital only an office building and devoted most of the site to housing, commercial space, and parking. Further, this plan called for demolishing all but the auditorium portion of the main building and demolishing the gymnasium.

On April 4, 1990, an architectural firm submitted a feasibility study of developing the site on behalf of Children's Hospital. This study, which retained the main building, included space for administrative offices, a child care center, an educational/conference center, and a medical research center. This study concluded that this project would cost an estimated \$3.7 million dollars less than what it would cost to construct a new building with comparable interior and exterior space. However, this project did not include retail space. On the same day that the architectural firm submitted its feasibility report, Children's Hospital withdrew from negotiations with the city and its developer. Children's Hospital told the city that it was not interested in participating in a project that would eliminate the facade of the old buildings or in participating in a combined use project.

Although both of the projects discussed above appear to be mutually exclusive, if the city was committed to preserving the main building, including the auditorium, it appears that an economically feasible project could be developed that would allow for that preservation. In fact, the main building covers less than half of the nine-acre site, leaving substantial space for new construction if the main building could not be economically refurbished to house some uses. However, we have not had sufficient time to review the building codes and regulations that would govern different types of construction or uses, or to conduct a thorough cost analysis.

Whether the Property Is
Adequately Protected from
Vandals and Deterioration

The National Historic Preservation Act of 1966 requires the city to protect historic properties that it owns. We were unable to determine whether the buildings at the site have suffered deterioration or damage as a result of the city's failure to protect them because we do not know what condition the buildings were in when the city acquired them. Further, according to an historian at the Office of Historic Preservation, they have not made a site visit to assess the degree to which the city has protected the buildings because they too do not have a record of the buildings' condition when the city acquired them. Nevertheless, we did find evidence that, in the past, the city has not always ensured the security of the buildings. For example, on April 24, 1989, after receiving a call from a concerned citizen, the city's assistant fire marshal visited the site to inspect for possible fire hazards. The marshal noted that, although two double yard gates were secured with pad locks, there was enough slack in the chain to allow a person to squeeze through the gates. Among other problems, the marshal also noted that the building was filled with highly combustible rubbish and concluded that the conditions constituted a serious fire hazard. The existence of these conditions show that the city was not fully protecting the property. In addition, in December 1989, the HUD's Office of Inspector General concluded that the city belatedly took action to address safety concerns at the project after the matter was brought to its attention.

We visited the site with members of the city's staff and a representative from the Office of Inspector General on October 2, 1990. Although the buildings appeared to be secure, there was evidence that someone recently had made an unauthorized entrance. For example, city staff noted that recently someone had torn lockers from the walls on the second floor of the main building. In addition, we noted a pile of debris inside an entrance to the gymnasium. City staff commented that the material had not been there less than one week before. We tried all of the doors at the ground level and found none open.

The Ability of the Developer
To Complete the Contract

Although we did not find evidence that the developer is unable to complete the project, we did note that the two principal parties in the development firm did not always honor their financial obligations in their early dealings with the city. However, the developers more recent financial activities with the city have been more favorable.

As noted in the city manager's letter to the Joint Legislative Audit Committee, the city's auditor reviewed the developer's ability to complete the project. She did this at the request of a city council member who was concerned that there may have been legal relationships between the developer and a corporation that had filed for Chapter 11 bankruptcy that might result in liens and attachments on the Martin Luther King, Jr. Community Plaza project. The city's auditor stated that such issues are legal matters and, as auditors, the city's auditors were unable to respond to that question.

The city auditor also reviewed the history of three agreements between the city and the two principal parties in the developer's firm. One of these agreements was with the developer for the Martin Luther King, Jr. Community Plaza project; the other two agreements were HUD loans given to the same two individuals for another business. In her report, dated May 8, 1990, the auditor stated, "in selecting a developer for any given project, it is prudent for the selection committee to" consider the developer's past performance in delivering products or services in a timely manner and the developer's past adherence to the responsible business practice of honoring financial obligations. The auditor reported that the first criterion did not apply to the loans because the agreements did not require the timely delivery of an end product. She further reported that the developer has not been able to move forward with the project because of unresolved differences in the initial development proposal, because of local opposition, and because of the need for extensive environmental and historical reviews.

With regard to honoring financial obligations, the auditor noted that, for the first loan, made in 1983, the two parties' business did not consistently adhere to the responsible business practice of honoring their financial obligations in a timely manner. Specifically, the borrowers made loan payments late in 44 (58.7 percent) of 75 months. In addition, the borrowers were to have made an interest payment of \$10,196 on December 13, 1983. However, the borrowers did not make this payment until seven months after the due date.

For the second loan, made in 1987, the borrowers made their payments on or before the due date and retired the loan in 1989. The city's auditor also reported that the developer honored its financial obligations related to the Martin Luther King, Jr. Community Plaza project. However, according to correspondence between the city and the developer, the developer did not provide \$60,000 in deposit fees required as a condition of its exclusive agreement. The fees, covering February through July 1988, were not paid to the city until July 20, 1988. On August 20, 1990, the city committed itself to negotiate exclusively with this developer through February 16, 1991; on September 4, 1990, it received a \$50,000 letter of credit as a deposit from the developer.

Whether It Is in the Best Interest of the
City To Grant More Time to the Developer
To Complete the Project, To Issue a
New RFQ, Or To Sell the Property

There was insufficient time for us to determine whether it is in the best interest of the city to grant more time to the developer, to issue a new request for qualifications, or to sell the property. However, as stated above, the city has obligated itself to negotiate exclusively with the current developer through February 16, 1991. Under any plan to continue with the project, it will take the city a long time before it completes the Martin Luther King, Jr. Community Plaza. According to the city, the developer will present a new project plan to the public on October 19, 1990. This plan will save and refurbish the auditorium, but will demolish the rest of the main building and the gymnasium. Even if this project plan goes forward, the city still will have to perform an environmental site assessment process, meet with the community for input regarding the plan, execute a further agreement with the developer, obtain a memorandum of agreement from the National Council on Historic Preservation that will allow the city to demolish portions of the main building and the gymnasium, and obtain zoning and other approvals for the project--all before beginning construction.

According to an analysis of appropriations and expenditures prepared by the city's Office of Economic Development and Employment staff, the city has spent over \$1.9 million on this project as of August 31, 1990. This amount includes approximately \$460,000 used to acquire the property, over \$910,000 for professional services, and over \$358,000 for city staff and related costs. The city paid over \$600,000 of the \$910,000 spent on professional services to the firm discussed on page 2. As of August 1990, the project manager estimated that the project will cost an additional \$840,000 over the next four years, not including the cost of construction. Because of time constraints, we were unable to validate the city's analysis nor to determine how much if any the city has paid to the current developer.

Whether the City's RFQ
Process Was Adequate

As we reported on page 2, the city received two responses to its September 1987 RFQ. We reviewed the selection criteria and rating sheets completed by the selection committee and found that the final selection was supported by the numerical ratings given. However, due to a lack of records, we were unable to confirm that the city solicited statements of qualifications from more than two prospective developers. In addition, the HUD's Office of Inspector General reviewed the city's RFQ process and concluded that there was no

Honorable Elihu Harris, Chairman
Members, Joint Legislative Audit Committee
October 15, 1990
Page 8

P-032

substantive evidence that the selection process was unfair, but that the city did not use newspapers to solicit proposals and did not keep complete documentation of its process.

RECOMMENDATIONS

We recommend that the Joint Legislative Audit Committee amend the approved audit to focus our work on the following two areas:


- Whether it is economically feasible to refurbish the main building and the auditorium, and
- Whether it is in the best interest of the city to grant more time to the developer to complete the project, to issue a new request for qualifications, or to sell the property.

However, the answers to those questions involve not only economic considerations, but historic preservation and community desires. It is unlikely that we can give a definitive answer based on anything but economic considerations.

We do not recommend any additional work related to the following three areas:

- Whether the property is adequately protected from vandals and deterioration. The lack of documentation regarding the condition of the buildings when the city acquired them would severely limit any analysis of deterioration or neglect.
- The ability of the developer to complete the contract. This question arose as a result of another firm with which the developer is related filing for Chapter 11 bankruptcy. As the city's auditor stated, this is primarily a legal question related to corporations; and,
- Whether the city's process for selecting its developer was adequate because of the lack of records that would provide any additional information.

Respectfully submitted,


KURT R. SJOBERG
Acting Auditor General

CITY OF OAKLAND



CITY HALL • ONE CITY HALL PLAZA • OAKLAND, CALIFORNIA 94612

Office of the City Manager
Henry L. Gardner
City Manager

415 273-3301
TDD 839-6451

UG 13 70

Honorable Elihu Harris, Chairman
Joint Legislative Audit Committee
State Capitol, Room 2148
Sacramento, CA 95814

Dear Assemblyman Harris:

SUBJECT: Request by Assemblyman Tom Bates for an audit of the
Martin Luther King, Jr. Community Plaza Project

The purpose of this letter is to respond to the request made to you from Assemblyman Tom Bates for an audit of the Martin Luther King, Jr. Community Plaza (MLK) Project, formerly the Merritt College campus site.

The City of Oakland strongly objects to a State audit on the grounds that no State money has been contributed to the MLK Project. It should also be noted that at no time has the Project Manager, or any staff related to the MLK Project, been contacted by Assemblyman Bates' office regarding his questions and concerns.

The MLK Project is a proposed mixed use development project. The elements of the plan were developed in response to a year-long community input process designed to determine the needs of the nearby community in relation to development opportunities for this nine acre site. There was consensus among community participants that there is a need for a grocery store, senior services, child care and other retail and convenience services in the neighborhood. The respondents also indicated that they would prefer complete or partial retention of the main building if possible.

Assemblyman Bates requested that the Auditor General specifically examine the following issues:

- o Whether it is economically feasible to refurbish the main building and auditorium.

The extent of improvements required, and the associated costs of refurbishing the main building will depend upon its usage. For example, structural and mechanical building codes are more stringent for public facilities than for office space. The economic feasibility of

various development plans will also depend upon the risk assumed by whomever develops the property. The feasibility of refurbishing the main building for retail use was investigated by consulting engineers. It was deemed unfeasible to refurbish the main building, due to its deteriorated state, and the costs of bringing the building up to seismic code.

Retention of the auditorium will be included in the development plan.

- o Whether the property is adequately protected from vandals and deterioration.

An eight (8) foot cyclone fence surrounds the property, and "No Trespassing" signs are posted on the fence. All doors, windows and roof openings in the main building, auditorium and gymnasium have been boarded up. While the doors and windows of the Mechanical Arts annex are boarded, the skylights are not, due to insufficient funds at the time the contracts were let. Additional funding has been subsequently secured, and this work will be performed by the end of August.

A security company patrols the site daily to detect signs of trespassing and vandalism. Board-up contractors are on call to reboard any openings in the buildings that occur, within 24 hours of notification (except on weekends). "Unsafe Building" signs are posted around each of the buildings to warn trespassers of the danger of entering.

A grounds crew visits the site regularly to cut weeds and pick up debris. A graffiti abatement crew painted over the exterior walls of all the site's buildings in May, 1990.

- o The ability of the developer to complete the contract.

The question of North Oakland Redevelopment Associates' (NORA) ability to fulfill the obligations of the proposed development plan was investigated by Oakland's City Auditor. The results of that investigation found no conclusive evidence that NORA could not fulfill the obligations of the project.

- o Whether it is in the best interest of the City to grant more time to the developer to complete the project, to issue a new RFQ, or sell the property.

The City of Oakland is confident of its ability to determine its own best interest. Each of the options mentioned above were analyzed in terms of tasks involved, associated costs and meeting community objectives. Based on these analyses, the Oakland Redevelopment Agency voted to continue with the proposed development plan.

- o Whether Oakland's RFQ process was adequate.

Since U.S. Department of Housing and Urban Development (HUD) money was used to acquire the site, HUD representatives evaluated the City's Request for Qualifications (RFQ) process, and found it to be adequate. The City was asked by HUD to advertise future RFQ's in local newspapers, however.

I trust this responds to the concerns raised by Assemblyman Bates. If you have any further questions, please feel free to contact me at (415) 273-3305, or Janice Lang, Project Manager at (415) 273-3692.

Sincerely,


For HENRY GARDNER
City Manager

cc: Assemblyman Tom Bates